CML Healthcare Inc.






Health Care is People Care®






2002
Annual Report

Health Care is
People
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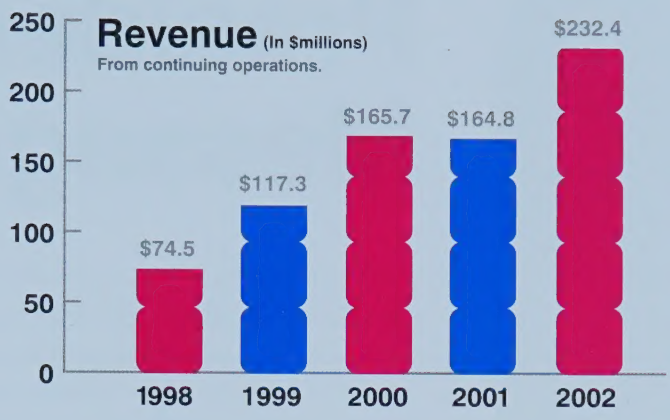
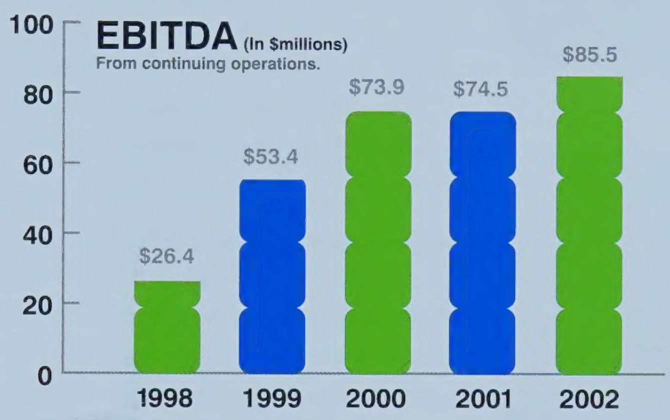
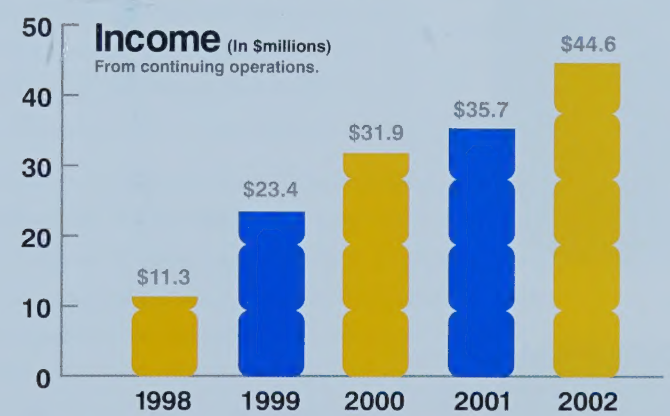
"In addition to significant achievements within both of our core operating businesses, CML once again delivered strong year-over-year financial performance."

John D. Mull, M.D., F.R.C.P. (C)
President and CEO







Year In Review:

- Completed acquisition and administrative integration of DC DiagnostiCare Inc.
- Achieved record revenue and earnings from continuing operations
- Divested U.S. pharmaceutical research business
- Filed Investigational New Drug (IND) applications for a sustained release Tramadol and a formulation of Isotretinoin
- Subsequent to fiscal year-end, submitted New Drug Application (NDA) for Fenofibrate

President's Message

In my report to shareholders for the fiscal year 2001, we introduced CML's acquisition of DC DiagnostiCare Inc., a transaction we believed would be accretive to earnings in its first year following the acquisition date and would provide CML with a national presence to further expand its healthcare and diagnostic business. By integrating our laboratory testing business with the acquired medical imaging business, our initial goal was to reduce total costs at DC DiagnostiCare by in excess of $2 million annually. Once these immediate costs savings were recognized, we could begin to strategically realign clinic locations while searching for additional acquisition opportunities.

As a result of a cooperative effort from both teams, CML accomplished its integration plan in 2002 well ahead of our own internal expectations. As expected, the acquisition was accretive within the first year and, through the realization of synergies and savings in the areas of finance, administration and the elimination of certain public company costs, we were able to create annualized cost savings of $2.8 million, exceeding our initial target of $2 million. In fact, the integration of these two operations was so successful we have already begun the process of consolidating clinics into diagnostic centres while we investigate new technologies better able to efficiently serve the needs of patients.

We believe the medical imaging market continues to provide a very significant opportunity for CML as DC DiagnostiCare currently occupies less than 10% of the non-hospital based imaging market in Canada and less than 5% of the total Canadian imaging market – a market which is growing at a rate of approximately 5% per annum. Although some organic growth will be realized, much of our growth in this area will come from the acquisition of additional medical imaging businesses across Canada.

Our decision to enter the medical imaging business was more than opportunistic; we see it as a further reflection of our fundamental belief that "Health Care is People Care". We believe that patients across the country can be better served by diagnostic centres that offer a wide range of services under one roof. In the future, we will leverage our national platform to add additional diagnostic services, cost effectively and delivered to high quality standards.

As we continued to focus internal resources on the execution of our growth strategy for the Healthcare and Diagnostic Division, CML made the decision in our third fiscal quarter to divest our U.S. Site Management Organization (SMO) as it was deemed a non-core business. CML first entered the U.S. pharmaceutical research business through the acquisition of Summit Research Network in January of 1999 and subsequent to the year ended September 30, 2002, we completed the sale of the business to a purchasing syndicate made up of current Summit management. In our fiscal 2002 financial statements we have taken a full provision for the orderly wind-up of two remaining research sites not included in the transaction and management is currently evaluating all of our options.

As a result of this divestiture, CML did incur certain one-time costs that impacted our earnings at the end of fiscal 2002. However, we are confident that this transaction provided the most cost effective means to exit this non-core business. With the disposal of the U.S. SMO business, management will be better able to focus on our core Healthcare and Diagnostic business.

Within our Pharmaceutical Division, we will continue to provide pharmaceutical research services in Canada through our wholly-owned subsidiary Pharma Medica and will continue to develop novel drug products through another wholly-owned subsidiary, Cipher Pharmaceuticals. 2002 was another exciting year of achievement for Cipher as we continued to move our clinical programs forward while strengthening our senior management team. During the year Cipher filed two additional Investigational New Drug (IND) applications for a sustained release version of Tramadol and a formulation of Isotretinoin and, perhaps Cipher's most significant achievement to date was its submission of a New Drug Application (NDA) for Fenofibrate with the U.S. Food and Drug Administration (FDA) in December of 2002, after the fiscal year-end.

In addition to significant achievements within both of our core operating divisions, once again CML as a whole, delivered strong year-over-year financial performance. Fuelled by the inclusion of three full quarters of the acquired business from DC DiagnostiCare, revenue from continuing operations at CML grew by 41% to $232.4 million for the year ended September 30, 2002 up from revenue of $164.8 million a year earlier. Income from continuing operations was also positively impacted, growing by 25% from $35.7 million in 2001 to $44.7 million in 2002.

Moving into fiscal 2003, CML remains well positioned within the landscape of Canadian healthcare. Our Healthcare and Diagnostic Division will continue to be our primary focus as we search for opportunities to acquire clinics which provide access to new geographic markets or complementary diagnostic services.

This evolution in our business strategy has mandated a change in corporate identity and as a result we are asking shareholders to vote to approve the amending of our corporate name to CML Healthcare Inc. at our Annual and Special Meeting of shareholders on March 26, 2003. The new name combined with a new marketing identity will more effectively position CML as it strives to become a leading North American healthcare services provider.

On behalf of the board, I would like to once again thank all of our shareholders, employees and patients who continue to support our vision for healthcare in Canada.

Yours truly,

John D. Mull

John D. Mull, M.D., F.R.C.P. (C)
President and CEO

From top to bottom: Dr. John D Mull, M.D. F.R.C.P. (C) - President & CEO
Paul J. Bristow, CA - CFO

Report on Operations:

Healthcare and Diagnostics

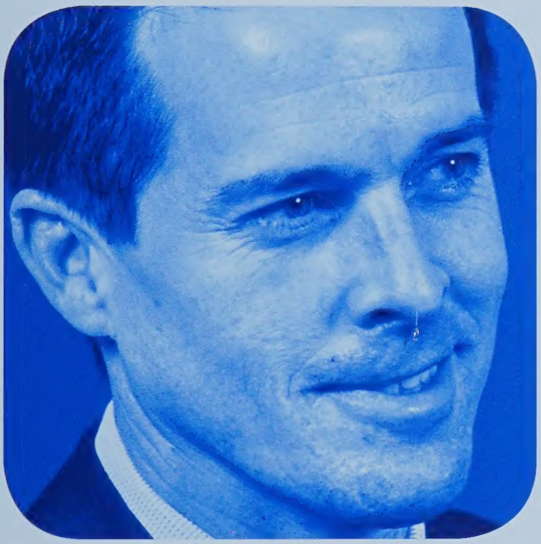
On November 30, 2001, CML completed the acquisition of DC DiagnostiCare Inc., the leading provider of non-hospital based medical imaging services in Canada. Through the acquisition of DC DiagnostiCare, CML immediately gained access to a non-capped market estimated at $1.8 billion per annum in Canada.

At the time of the acquisition, DC operated 146 clinics across five provinces in Canada generating approximately $70 million in annual revenue. This represents less than 5% of the total medical imaging market in Canada and less than 10% of the non-hospital based market.

In 2002, CML immediately began the process of integrating DC DiagnostiCare's medical imaging operations into its existing laboratory testing business in Ontario. Both businesses are complementary sharing many of the same characteristics and requiring interaction with the same participants, namely: provincial governments, patients and physicians. CML's long history in the private delivery of diagnostic laboratory services in Ontario has aided the integration process, resulting in its timely completion well ahead of budget.

By reducing corporate expenses including bank syndicate fees, administration and certain public company costs, CML has been able to generate significant cost savings. Further cost savings will be achieved through the consolidation of certain sites creating diagnostic centres that offer both laboratory testing and medical imaging services.

In an effort to generate the greatest efficiencies and to promote joint strategic planning and implementation, senior management from both the laboratory testing business and the medical imaging business have been integrated at the Company's main facility in Mississauga, Ontario. Subsequent to the end of its fiscal year, CML further strengthened its Healthcare and Diagnostic team with the appointment of Kent Wentzell as General Manager, Medical Imaging in October of 2002.



...access to a non-capped market estimated at $1.8 billion per annum...

Pharmaceuticals

During fiscal 2002, CML's wholly-owned drug development company Cipher Pharmaceuticals continued to advance its clinical programs. Beginning in the first quarter of fiscal 2002, Cipher finished phase I testing of a novel formulation of Fenofibrate and subsequent to the end of the fiscal year, Cipher submitted its first New Drug Application (NDA) with the FDA for Fenofibrate.

In fiscal 2002, Cipher filed Investigational New Drug (IND) applications with the FDA for a sustained release version of Tramadol and for a formulation of Isotretinoin. Both products are currently undergoing clinical testing.

To fund these positive clinical developments including ongoing clinical trials of Cipher's fourth product, a novel formulation of Budesonide, CML invested $9.7 million in research and development for the fiscal year ended September 30, 2002. CML expects to invest between $15 and $17 million for the fiscal year ended September 30, 2003.

While CML's drug development business was making steady progress in 2002, CML decided to exit its U.S. pharmaceutical research business. After an in-depth analysis of all internal options, CML made the decision to divest this non-core business in the summer of 2002.

In November of 2002, CML completed the sale of its majority ownership in Summit Research Network Management, Inc. to a syndicate made up of current management. As a condition of the transaction, CML retained ownership of two research sites located in Colorado and Florida. The Company has taken a full provision for the orderly wind-up of these two remaining sites in its financial statements for fiscal 2002 and currently management is evaluating all of its options.

CML will continue to operate and support Pharma Medica Research Inc., its wholly-owned Canadian pharmaceutical research business.

From top to bottom: Dr. Ian French – Chairman & Chief Scientific Officer, Cipher Pharmaceuticals Limited
Craig Mull – Director of Corporate Development

CML Healthcare

An Evolution

A National Provider of Healthcare and Diagnostic Services

For over 30 years, Canadian Medical Laboratories Limited (CML) has operated under the vision that "Health Care is People Care". In that time, CML has grown from a single physician-operated laboratory to a national network of facilities that provides millions of Canadians with quality and dependable diagnostic services. In Ontario, CML performs over 100,000 specimen tests each day and services over 450,000 patients at 195 facilities each month. This expertise in specimen testing is complemented by an array of imaging services including: Ultrasound, X-Ray, Fluoroscopy, Mammography, Bone Densitometry and Nuclear Medicine. In Alberta and British Columbia, CML is also a leading operator of clinics providing Magnetic Resonance Imaging (MRI) services.

Founder and Key Business Units

In 1971, John D. Mull, M.D., F.R.C.P. (C), a pathologist, founded CML to provide physicians and their patients with dependable and reliable patient-focused diagnostic laboratory services. This approach, coupled with several strategic acquisitions, has allowed CML to expand beyond diagnostics into pharmaceutical research and drug development. The Company is divided into two principal operating divisions:

- **Healthcare and Diagnostic – comprised of laboratory testing and medical imaging operations; and**
- **Pharmaceutical – comprised of pharmaceutical research and drug development operations.**

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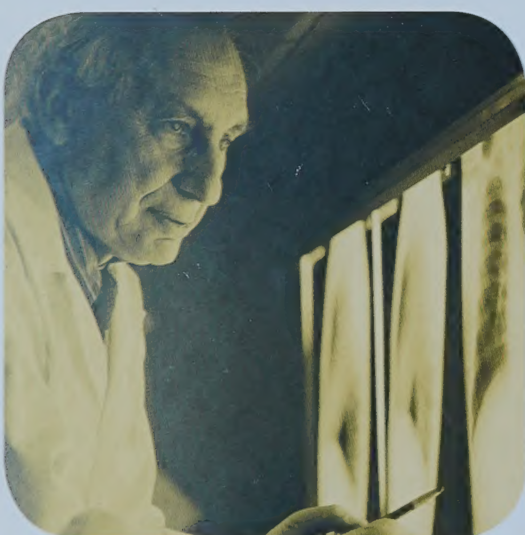
Supported by this strong and successful history, management and the board of CML are proposing a transformation of the Company's brand identity to better reflect its current and future growth opportunities.

At the Company's Annual and Special Meeting of shareholders on March 26, 2003 the Company will be asking the shareholders of CML to vote to change the name of the corporation. The proposed name of the corporation, CML Healthcare Inc., will more properly represent the scope and breadth of the services the Company is offering today and will recognize the corporation's 30 years of development into a first-class healthcare services company.

Canadian Medical Laboratories Limited has been using the name CML Healthcare for the past twelve months for internal operational purposes and the Company's new corporate website resides at the address www.cmlhealthcare.com.

As the landscape of North American healthcare continues to evolve brand identity will become increasingly important for patients and referring physicians. Management and the board of directors of CML believe that the Company must evolve as well.

In Ontario, CML performs over 100,000 specimen tests each day...



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CML Diagnostics

Services

CML's vision of "People Care" has consistently allowed CML to deliver the latest medical diagnostic services in a cost-effective manner. This focus on bringing high quality healthcare to the patient has allowed CML to successfully expand this vision, first within Ontario and then beyond, while also allowing CML to succeed as a business. Maintaining this important balance has permitted the Company to access the capital markets – not the taxpayer – in order to fund a growing array of high quality healthcare services for Canadian patients and their attending physicians.

CML's Healthcare and Diagnostic Division delivers a comprehensive range of laboratory testing and medical imaging services such as:

Medical Imaging

Ultrasound

Ultrasound imaging utilizes high-frequency sound waves to develop images of internal organs, unborn fetuses and the vascular system. Ultrasound has widespread applications, particularly for procedures in obstetrics, gynecology and cardiology.

Magnetic Resonance Imaging (MRI)

Magnetic Resonance Imaging (MRI) is a painless and non-invasive examination which takes pictures of the inside of the body. MRI uses a tunnel-shaped magnet to set up a strong magnetic field around a patient. With MRI, doctors can detect certain conditions earlier and more easily, thus allowing more effective treatment and possibly eliminating the need for surgical procedures.

Mammograms

Mammography is a specialized form of radiology utilizing low dosage x-rays to visualize breast tissue and is the primary screening tool for breast cancer. Mammography procedures also include the non-invasive biopsy of cells to assist in the diagnosis of breast cancer.

Bone Densitometry

Bone Densitometry is currently accepted by the Osteoporosis Society of Canada as being a quick, simple, painless examination that is currently the most sensitive screening tool used to detect bone loss in the early stages of osteoporosis.

X-Ray

X-rays utilize roentgen rays to penetrate the body and record images of organs and structures on film. Fluoroscopy utilizes ionizing radiation combined with a video viewing system for real time monitoring of organs. X-ray and fluoroscopy are the most frequently used imaging modalities.

...the latest medical diagnostic services in a cost-effective manner.

Laboratory Testing (Ontario)

Hematology

International Normalized Ration (INR) is a blood clotting test. With the widespread use of blood thinners in heart patients, this test is used to monitor the medication prescribed by the physician.

Biochemistry

Prostate Specific Antigen (PSA) is a chemical analysis to determine the level of PSA in the blood. This assists the physician in the diagnosis and treatment of prostate cancer in men.

Cytology

Cervical smear (pap smear) is the microscopic examination of cells to determine the presence of cancerous or precancerous cells. This test assists the physician in the early detection of cervical cancer in women thus helping assure successful treatment.

Microbiology

Culture and Sensitivity (C&S) is the finding and identifying of a disease producing bacterium in the body and determining the antibiotic required for treatment.

Histology

Histology testing is the preparation and examination, by a pathologist, of surgically removed tissues to detect disease conditions such as skin cancers and psoriasis.

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CML Diagnostics

People behind the Vision

1,800 people at CML's Healthcare and Diagnostic Division achieve the vision of "Health Care is People Care" through the delivery of high quality service, keeping the priority of patients first. It is this philosophy that has fuelled the success of the Company since its formation in 1971.

Donald Kerr,

General Manager, Laboratory Services

Don Kerr has served as CML's General Manager of Laboratory Services since 1997. Prior to his appointment at CML, Mr. Kerr held the position of General Manager at Dr. T.A. Kasper and Associates Medical Laboratories where he was employed for 24 years.

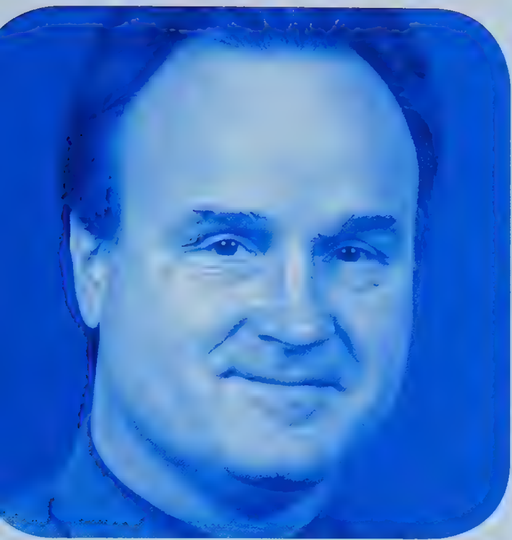
"Having devoted more than 30 years of my life to the healthcare field, I am particularly pleased to play a role in the benefits patients will enjoy as a result of our acquisition of DC DiagnostiCare. By combining a wide range of diagnostic services under one roof, CML Healthcare will provide one-stop patient access for most common testing procedures. In addition, with the introduction of new technologies and state-of-the-art procedures we will be able to shorten the time patients and their physicians have to wait for results, improve overall efficiency and reduce costs."

Dr. Murray Miskin, M.D., F.R.C.P. (C)

Consulting Radiologist

Dr. Miskin was a founder of MCTU, a medical imaging company previously acquired by DC DiagnostiCare. His role as a radiologist involves interpreting results and diagnosing patients based on x-ray and imaging results.

Dr. Miskin says he absolutely loves his job: "I can't wait to get in to work in the morning."



...always keeping the priority of patients first.

Kent Wentzel,

General Manager, Medical Imaging Services

Mr. Wentzell was appointed General Manager, Medical Imaging at CML in October of 2002. He brings to CML a wealth of senior management experience supported by 14 years in the diagnostic imaging fields where he held positions in marketing, sales and service and 10 years in the area of laboratory diagnostics.

"I am very excited about the prospects for leveraging CML's Healthcare and Diagnostic Division's national presence to deliver high quality diagnostic services to communities across Canada."

Beverley Batchellor,

Sonographer

Beverley is a Sonographer, having worked at the busy Yonge St. office for the past 15 years. The work performed at this office is quite diverse, including high risk obstetrical examinations, as well as infertility, gynaecological, cardiac, vascular, general abdominal and small parts examinations.

"I enjoy the close working relationship with my colleagues. The recent addition of new generation equipment has added to the quality and efficiency of our work."

CML Diagnostics

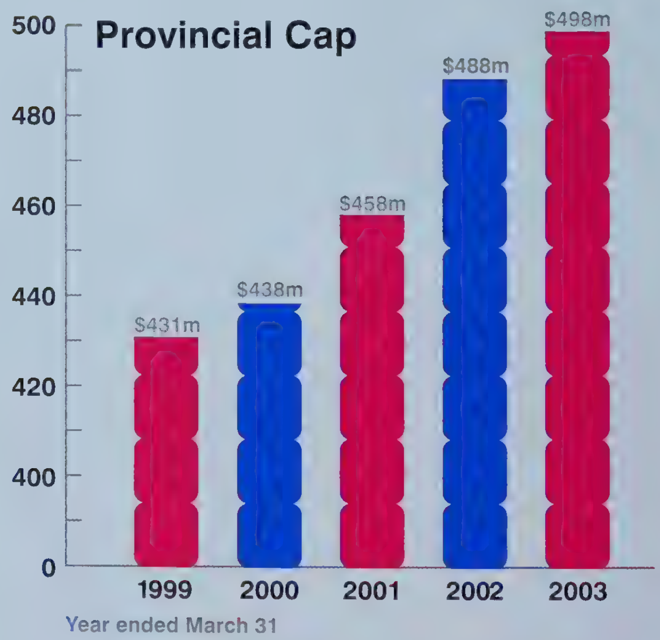
Market Opportunity

Laboratory Testing Services

For the year ended March 31, 2003 the provincial payment cap for laboratory testing services in Ontario is $498 million. CML currently holds approximately 30% of the Ontario laboratory testing market. This funding is provided by the Ontario Ministry of Health (MOH) pursuant to an agreement between the Ontario Association of Medical Laboratories (OAML) and the MOH. The current agreement expires on March 31, 2003.

Currently CML offers laboratory services only in the province of Ontario, which represents the largest provincial market for laboratory testing services in Canada.

Over the past five years the provincial cap has increased steadily as laboratory testing volumes have increased considerably.



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In addition to laboratory fees paid by the provincial government, CML does perform non-MOH funded services as well.

Medical Imaging Services

The medical imaging services market in Canada is estimated at over $1.8 billion per annum with estimated growth of approximately 5%. Approximately 56% or $1.0 billion in medical imaging services are performed at hospitals in Canada with the remaining $800 million being non-hospital based. As with the laboratory testing services in Canada, Ontario represents the largest market segment.

Given CML's 2002 medical imaging revenue, CML diagnostics currently occupies less than 4% of the Canadian market.

Building a Strong Canadian Presence

CML now offers patients and physicians quality services in five provinces across Canada through a network of approximately 350 facilities.

CML Diagnostics

Future Outlook

Healthcare spending in Canada continues to increase each year. In 2001 health related expenditures in Canada rose 7.2% to $97.6 billion up from $91 billion in 2000. 70% of healthcare expenditures in Canada is financed from public funds and the remaining 30% is financed from private sources. Many factors contributed to the increase in spending over the past several years, however, one dominant factor continues to be the aging population.

Despite many new provincial healthcare spending initiatives, public health facilities are continually being pressured to reduce or control costs. As a result, private health facilities are providing an increasing number of health services to Canadians.

CML will continue to play a key role in the delivery of a growing number of healthcare services to Canadians. CML has made considerable investments in the capital equipment and infrastructure required to efficiently deliver these services which, along with provincial licenses to operate its facilities, acts as a considerable barrier for new market entrants.

With the administrative integration of DC DiagnostiCare complete, CML is now focused on building on its existing platform of services and enhancing the delivery of these services by introducing new technologies:

- **Tele-radiology which enables the electronic transfer of large imaging files. In the future, this new technology will allow for more efficient delivery of the service and convenience for the patient, while significantly reducing processing costs; and**
- **Cmldiagnostics.com a robust corporate web interface focused on providing timely information to patients and physicians. Through cmldiagnostics.com, patients will be able to better prepare for examinations, schedule appointments and locate clinics, while physicians will be able to view test results immediately – without the need to wait for paper delivery. The first phase of the cmldiagnostic site is expected to be launched in fiscal 2003.**

In addition to new technologies, CML continues to search the Canadian and U.S. markets for acquisition opportunities which build on CML's core competencies and once integrated, will deliver attractive return potential. These new acquisition opportunities may provide access to new geographic markets or may add to the Company's comprehensive array of diagnostic services.

In 2001 health related expenditures in Canada rose 7.2% to $97.6 billion...

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Management's Discussion & Analysis

The following is a discussion and analysis of the operating results and financial position of Canadian Medical Laboratories Limited (CML or the Company) for the fiscal year ended September 30, 2002. This document should be read in conjunction with the consolidated financial statements, including the notes thereto, appearing elsewhere in this Annual Report

Overview:

The Company operates within two dominant business segments/divisions: Healthcare and Diagnostic, and Pharmaceutical.

Healthcare and Diagnostic Division

This division includes the Company's laboratory testing business and the medical imaging business. The imaging business has been added through the acquisition of DC DiagnostiCare Inc. (DC) during Fiscal 2002.

Effective November 29, 2001, CML acquired approximately 88.1%, or 23,403,721 of the outstanding common shares of DC. The shares were acquired at $0.60 per share, for a cost of $14.0 million. Also, CML purchased all of the indebtedness owing by DC to its banking syndicate together with the 53,620,217 warrants held by the syndicate to purchase an equivalent number of common shares of DC for an amount equal to the debt owing at the time of purchase plus $1.0 million. The debt owing at the time of purchase was $33.0 million. In order to obtain greater than 90% of the outstanding shares of DC, CML extended its offer to December 21, 2001. On December 21, 2001, the Company announced it had acquired an additional 1,515,235 common shares of DC, to increase its total holdings to 93.4%. On March 15, 2002 CML acquired the remaining 1,761,469 outstanding shares of DC. The results of DC from November 29, 2001 onward are included in CML's September 30, 2002 financial statements.

Effective May 31, 2002 the DC head office operations were transferred from the Edmonton office to CML's Mississauga office. This combined with other synergies already recognized resulted in annualized savings of $2.8 million.

Management's Discussion & Analysis

During the last quarter of this fiscal year, in accordance with Generally Accepted Accounting Principles (GAAP), the Company completed the determination of the fair market values of the acquired net assets. The significant adjustments were as follows:

- **Reduction of $13.8 million in the value assigned to property and equipment, resulting in a credit to amortization expenses of $1.1 million for the fourth quarter of 2002.**
- **Reduction of the future tax liability of $10.0 million mainly related to the recognition of DC's non-capital loss carryforwards.**
- **Provisions for accounts receivable of $1.3 million.**

These adjustments were to the balance sheet acquired and therefore, there was no current year earnings impact from these writedowns with the exception of recalculating amortization expense on a lower base.

Pharmaceutical Division

This division includes the drug development business carried out by Cipher Pharmaceuticals Limited (Cipher), and the pharmaceutical research business consisting of Pharma Medica Research Inc. (Pharma).

Cipher continued its clinical trials for a sustained release version of Tramadol, a pain reliever, and Budesonide, a prophylactic treatment for asthma. Cipher met with the Food and Drug Administration (FDA) to discuss its planned U.S. New Drug Application (NDA) filing for a novel formulation of Fenofibrate, used to lower serum lipid levels in the blood. The Company believes it will take up to the end of calendar 2003 for the FDA to review the NDA and render a decision for approval. In May 2002, Cipher also filed an Investigational New Drug (IND) application for a formulation of Isotretinoin, used in the treatment of severe acne, and has started clinical testing.

Discontinued Operations

In May 2002, the Company implemented a plan to dispose of its U.S. Site Management Organization (SMO) operations. This business consisted of sites in various states across the United States engaged in providing clinical research for Central Nervous System disorders. During the Company's third quarter, CML concluded the sale of the Hartford Research Group, a part of the SMO business. Subsequent to year-end, CML concluded the disposal of its interest in Summit Research Network Management Inc. (Summit), a U.S. SMO with research sites in Michigan, Oregon, Colorado, Florida and Washington. Under the terms of the agreement, CML contributed all of its shares in Summit to a purchasing syndicate made up of Summit's management group and has retained ownership of both the Colorado and Florida operations. Summit will continue to provide certain administrative services to the Colorado and Florida operations while CML continues to review alternative strategies, which may include the orderly wind-up of these two remaining sites.

All of the operating results, assets and liabilities related to the SMO business have been presented as discontinued operations for all financial periods covered in this report. The Company has reported a loss related to the disposal of these operations of $10.7 million in the September 30, 2002 year-end results.

An assessment of the fair value of the goodwill as at October 1, 2001 was finalized during the year, at which time it was determined that $19.7 million of goodwill was impaired. In accordance with the new requirements of the Canadian Institute of Chartered Accountants (CICA), which were adopted by the Company during 2002, this goodwill impairment loss (all of which related to the Discontinued Business) was charged to retained earnings.

Management's Discussion & Analysis

Review of operating results from continuing operations:

Revenue

(In millions of dollars):
Year ended September 30,

	2002	2001	$ change in 2002	% change in 2002
Healthcare and Diagnostic	227.1	160.0	67.1	41.9
Pharmaceutical	5.6	5.4	0.2	3.7
Consolidation entry	(0.3)	(0.6)	0.3	50.0
Total	232.4	164.8	67.6	41.0

The increase in revenue in the Healthcare and Diagnostic Division for the year ended September 30, 2002 was primarily due to:

- **The inclusion of DC's revenue since November 29, 2001.**
- **The increase in the corporate cap for the Ontario diagnostic laboratory industry and the recognition of one-time funding of $3 million during Q2 2002.**

CML's revenue recognition policy for Ontario diagnostic laboratory revenue is to recognize the lower of corporate cap or billings based on services performed. CML billed in excess of its corporate cap entitlement for the Ontario Ministry of Health and Long Term Care (MOH) year ended March 31, 2002. There was also an increase in non-cap billings.

For DC's revenues, CML's revenue recognition policy is to recognize net revenue based on services performed. Beginning in the third quarter 2002, with a restatement to prior periods, CML has netted the Ontario utilization discount against revenue, to be consistent with the accounting treatment of the Ontario laboratory revenue. Prior to the third quarter, DC reported this utilization discount as an expense. This reclassification has no impact on net earnings. For the year-ended September 30, 2002, the amount of this utilization discount was $2.0 million.

Pharma's revenue increased by $6.0 million over the prior year. However, a significant portion of Pharma's revenue is from a wholly-owned subsidiary which is eliminated upon consolidation. Pharma has seen an increase in third party billings.

Operating, General and Administrative (OG&A) Expense:

(In millions of dollars):
Year ended September 30,

	2002	2001	$ change in 2002	% change in 2002
Healthcare and Diagnostic	133.8	82.6	51.2	62.0
Pharmaceutical	3.7	7.6	(3.9)	(51.3)
Research and Development	9.7	0.8	8.9	1,112.5
Consolidation entry	(0.3)	(0.6)	0.3	50.0
Total	146.9	90.4	56.5	62.5

The increase in OG&A expenses in the Healthcare and Diagnostic Division was primarily due to the inclusion of DC's results.

Management's Discussion & Analysis

The research and development amounts represent the drug development costs of Cipher which have increased due to the ramp up of this business over the prior year. Also, included in this amount is an impairment provision for the Budesonide investment of $1.4 million. Management is reviewing its options regarding the development of this product and considers it prudent to provide for any potential writedown of its investment at this time.

Earnings from Continuing Operations Before Interest, Taxes, Depreciation and Amortization (EBITDA):

(In millions of dollars):
(EBITDA is a non GAAP measure)
Year ended September 30,

	2002	2001	$ change in 2002	% change in 2002
Revenue	232.4	164.8	67.6	41.0
Less: OGA expenses	137.2	89.6	47.6	53.1
Less: Research and development	9.7	0.8	8.9	1,112.5
EBITDA	85.5	74.4	11.1	14.9
EBITDA margin	36.8%	45.1%		

While EBITDA increased over the prior fiscal year, the EBITDA margin decreased. This decrease was a direct result of research and development costs associated with Cipher's increased activities over the prior year and the lower margins associated with the DC operations. However, there has been a continuous improvement in the DC margins over the previous quarters. Management plans to continue to improve these margins through the continuation of an integration plan that has already begun with the centralization of functions such as administration and accounting. The DC head office in Edmonton was closed during the third fiscal quarter which, combined with synergies already recognized, resulted in annualized savings of $2.8 million.

Interest Expense

(In millions of dollars):
Year ended September 30,

	2002	2001	$ change in 2002	% change in 2002
Interest expense	2.8	3.4	(0.6)	(17.6)

While long-term debt has increased, interest expense has decreased. This is the result of the dramatic reduction in interest rates over the last 12 months. For the year ended September 30, 2002 compared to the year ended September 30, 2001 average interest rates decreased by approximately 260 basis points.

Provision for Income Taxes

(In millions of dollars):
Year ended September 30,

	2002	2001	$ change in 2002	% change in 2002
Income taxes a % of Income before taxes	44.4%	43.8%		
Income tax expense	35.7	27.8	7.9	28.4

Management's Discussion & Analysis

The combined tax rate for the fiscal period ended September 30, 2002 was 39.5% compared to 42.5% for the fiscal period ended September 30, 2001. However, the Company's effective combined tax rates differs from these rates due to the following:

- **The research and development costs are not tax effected.**
- **Losses not recognized as a tax benefit.**
- **Impact of future taxes and the reduced combined tax rates in the future.**

The Company has $46.9 million in non-capital loss carryforwards expiring in 2005 to 2017. Of this amount $37 million relates to DC loss carryforwards.

Earnings Per Share (EPS):

Year ended September 30,

	2002	2001	$ change in 2002	% change in 2002
Net income from continuing operations (In millions of dollars)	44.6	35.7	8.9	24.9
Basic EPS	2.19	1.75	0.44	25.1
Diluted EPS	2.17	1.72	0.45	26.2

Effective October 1, 2001 the Company adopted the new CICA Handbook Section 3500 for determining diluted EPS (see Notes to the Financial Statements Note 8 - Earnings per Share for a more complete explanation). EPS has been positively impacted by the requirement by the CICA to terminate the amortization of goodwill and other indefinite life intangible assets.

Prior year diluted EPS has been restated to comply with these new rules.

Related Party Transactions:

In the normal course of business, the Company leases facilities from companies that are controlled by certain shareholders and officers of the Company. Rent expense of $1.3 million (2001 - $1.4 million) related to these leased facilities, measured at exchange amount, has been included in OG&A expenses.

At September 30, 2002 $0.4 million (2001 - $0.4 million) is due from a company controlled by certain shareholders and officers of the Company. This amount consists of a gross receivable of $0.7 million, net of a provision of $0.2 million (2001 gross - $0.6 million, provision - $0.1 million). This balance is the result of restructuring the acquisition of assets of Excel Bestview Laboratories that occurred concurrently with the Company going public in November 1996. The Company is currently making monthly mortgage payments on the property on behalf of the related party. This balance will be repaid when the mortgaged property is sold. The loan is non-interest bearing. The related party's share of the outstanding mortgage at September 30, 2002 is $0.7 million. Management estimates the recoverability to be approximately $0.4 million and therefore the Company will continue to increase its provision so long as it continues to make the payments on this mortgage.

Investment in Genetic Diagnostic Inc.(GDI):

The Company holds 1,900,000 common shares (14%) of GDI at September 30, 2002. The amount of this investment is $2.75 million and has been accounted for on a cost basis in accordance with GAAP. GDI is currently a development stage company. Management believes that GDI will successfully complete its development project and therefore, the investment is considered fully recoverable.

Intangible Assets:

Management performed an analysis at September 30, 2002 and determined that the fair values of the intangible assets are not impaired.

Management's Discussion & Analysis

Investment in Preferred Shares:

During Fiscal 2001, the Company's wholly owned subsidiary, Cipher Pharmaceutical entered into four agreements with Galephar Pharmaceutical Research Inc. (Galephar) to package, test, obtain regulatory approvals and market certain products in North and South America, the Caribbean and Bermuda. In accordance with the terms of the agreements, the Company has made investments in Galephar of $7.2 million (US $4.6 million). The Budesonide investment was provided for at September 30, 2002 in the amount of $1.4 million (US $0.9 million) as management is currently reviewing its options regarding the development of this product and there is a possibility this investment will not be recovered.

It is expected that an additional $1.9 million will be invested in Galephar during Fiscal 2003 relating to the other products in the portfolio.

Liquidity and Capital Resources:

Cash and cash equivalent balances at September 30, 2002 were $26.7 million and long-term debt totaled $61.3 million. This compares to $19.6 million and $43.8 million respectively as at September 30, 2001.

The Company's credit facilities are with a banking syndicate led by the Canadian Imperial Bank of Commerce. The following facilities are in place at September 30, 2002:

- **Five Year Term loan – The balance outstanding at September 30, 2002 is $21 million.**
- **364-Day acquisition revolver – This line was increased by $15 million to $60 million during the year in order to finance the DC acquisition. At year-end $38 million was owing.**
- **Operating line of $10 million – Not drawn on as at September 30, 2002.**

The increase in the long-term debt from September 30, 2001 to September 30, 2002 is due to the financing of the DC acquisition with debt and the inclusion of DC's capital lease obligations.

As a result of the Healthcare and Diagnostic division's strong cash flows, the Company was able to pay down $34 million of principal during the year, compared to $20 million during the previous fiscal year.

All of Cipher's research and development expenses were, and will continue to be, funded by current year internal cash flow.

Capital Expenditures:

Purchase of property and equipment assets amounted to $1.5 million for fiscal year 2002 compared to $1.0 million in the prior fiscal year.

Additionally, the Company received $9.2 million from the MOH as an allocation of the Replacement Medical Equipment Fund. This funding was made available to Independent Health Facilities (IHFs) to assist with the costs involved in replacing diagnostic imaging equipment and is non-repayable. The Company used these funds primarily towards the replacement of 34 ultrasound and 15 mammography units at various clinics within Ontario. For accounting purposes the grant was netted against the assets acquired.

Share Capital:

On January 11, 2002, stock options to purchase 275,000 common shares were granted with an exercise price of $22.50 per share. 110,000 of the options vested immediately, with 82,500 vesting in one year and the remaining 82,500 vesting in two years.

Management's Discussion & Analysis

Also, on June 6, 2002, 30,000 options were exercised at an exercise price of $6.35 per share; on August 22, 2002, 10,000 options were exercised at an exercise price of $6.35 per share and on September 25, 2002, 500,000 options were exercised at an exercise price of $5.00 per share.

Business risks:

Financial: A significant portion of the Company's revenues is received from the MOH and is therefore subject to political policy decisions. Any changes in the funding program could have a negative impact on the Healthcare and Diagnostic Division's financial performance. Management continues to closely monitor the situation, and is actively involved with the Ontario Association of Medical Laboratories' board of directors.

Growth: The Company has experienced significant growth over the past few years. This growth is expected to continue.

The integration of DC will continue to pose significant challenges. Management has a strategy in place however, and has contracted with outside sources to assist with the integration process.

Other: The Company's entry into the drug development industry carries with it the normal risks of diversification and the risks of not gaining regulatory approval and /or lack of commercial market penetration. However, management has worked to identify potential risks and believes its strategic model minimizes these exposures.

Outlook:

At the Company's Annual and Special Meeting to be held on March 26, 2003, the shareholders will be asked to approve a name change for the Company to CML Healthcare Inc. As a result of the recent evolution of the Company, the new name more accurately reflects the activities and scope of the Company.

Healthcare and Diagnostic Division:

With the acquisition and continuing integration of DC, management will focus on improving EBITDA margins by generating efficiencies with current operations and applying their strong management practices to the imaging business.

The MOH has announced that it will be allowing IHFs to expand their diagnostic services to include Magnetic Resonance Imaging (MRI) and Computed Tomography (CT) services. Licenses will be granted for 15 MRI and five CT machines through a request for proposal (RFP) process. The Company will be involved in this RFP process but the total costs associated with these MRIs and CTs will depend on its success with the RFP process. The capital and leasehold cost, per license, is estimated to be $2.5 million.

Finally, while the short term focus will be integrating DC and recognizing all possible synergies, CML management will also be preparing an acquisition strategy for the future.

As always, management will aggressively pursue growth opportunities only when convinced they will be beneficial to the shareholders of the Company.

Management's Discussion & Analysis

Pharmaceutical Division:

Drug Development Strategy:

Cipher will focus on obtaining regulatory approval for, and commercializing the drugs it has already in-licensed. The Company spent $9.7 million during fiscal year 2002 and intends to spend $15-17 million during fiscal year 2003 on drug development consistent with the original intention of spending up to $30 million over a three-year period. This compares to the $19 million for fiscal 2002 and $9 million for fiscal 2003 the Company had budgeted in September 2001. The Company also plans to invest an additional $1.9 million in Galephar related to current agreements during fiscal 2003.

Cipher has commenced out-licensing discussions with several potential commercial distributors for several of its products.

As Cipher out-licenses its current portfolio of drugs, the Company will look for new in-licensing opportunities.

Forward-Looking Statements:

To the extent any statements made in this document contain information that is not historical, these statements are essentially forward-looking. A forward-looking statement is subject to risks and uncertainties that may be general or specific. A variety of factors, many of which are beyond the Company's control, affect the operations, performance and results of the Company, and could cause actual results to differ materially from the expectations expressed in any of the Company's forward-looking statements. These factors include, but are not limited to, pending and proposed legislative or regulatory developments; intensifying competition, resulting from established competitors and new entrants in the businesses in which the Company operates; technological change; interest rate fluctuations and general economic conditions; the difficulty of predicting FDA and Canadian Therapeutics Product Directorate approvals, acceptance and demand for new pharmaceutical products; and fluctuations in operating results. Reference is made to the Company's filings with Canadian securities regulatory authorities for a further description of risks associated with the Company's operations. These and other factors should be considered carefully and readers should not place undue reliance on the Company's forward-looking statements. The Company does not undertake to update any forward-looking statement that is contained in this Annual Report.

Management's Discussion & Analysis

Selected Quarterly Financial Information

(millions of dollars, except per share amounts) (unaudited)

For the year ended September 30, 2002	Total YTD	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
Revenue from continuing operations	232,448	48,004	61,277	61,925	61,242
Income from continuing operations	44,636	9,863	11,806	10,736	12,231
Net income	33,261	9,809	11,376	5,910	6,166
Basic earnings per share					
Continuing operations	2.19	0.48	0.58	0.53	0.60
Discontinued operations	(0.56)	0.00	(0.02)	(0.24)	(0.30)
	1.63	0.48	0.56	0.29	0.30
Diluted earnings per share					
Continuing operations	2.17	0.48	0.56	0.51	0.59
Discontinued operations	(0.55)	0.00	(0.02)	(0.23)	(0.29)
	1.62	0.48	0.54	0.28	0.30
For the year ended September 30, 2001					
Revenue from continuing operations	164,841	40,610	39,873	39,114	45,244
Income from continuing operations	35,743	7,040	6,689	7,565	14,449
Net income	35,375	6,427	6,913	7,093	14,942
Basic earnings per share					
Continuing operations	1.75	0.34	0.33	0.37	0.71
Discontinued operations	(0.02)	(0.03)	0.01	(0.02)	0.02
	1.73	0.31	0.34	0.35	0.73
Diluted earnings per share					
Continuing operations	1.72	0.34	0.32	0.36	0.69
Discontinued operations	(0.02)	(0.03)	0.01	(0.02)	0.02
	1.70	0.31	0.33	0.34	0.72

Reclassification of Discontinued Operations

The above quarterly information has been reclassified, not restated, for the SMO business to be shown as a discontinued operation, and has been prepared for comparative purposes only.

Responsibility for Financial Statements

The management of Canadian Medical Laboratories Limited is responsible for the preparation and presentation of the consolidated financial statements in accordance with generally accepted accounting principles. The most significant of these accounting principles have been set out in note 1 to the consolidated financial statements. Financial statements are not precise since they include certain amounts based on estimates and judgements. Recognizing that the Company is responsible for both the integrity and objectivity of the consolidated financial statements, management has determined such amounts on a reasonable basis in order to ensure that the financial statements are presented fairly, in all material respects. Management has prepared the financial information presented elsewhere in the annual report and has ensured that it is consistent with the financial statements.

The Company's accounting procedures and related systems of internal control are designed to provide reasonable assurance as to the reliability of the financial information and that the Company's assets are appropriately accounted for and adequately safeguarded.

The Board of Directors is responsible for ensuring that management fulfills its responsibilities for financial reporting and is ultimately responsible for reviewing and approving the financial statements. The Board is assisted in exercising its responsibilities through the Audit Committee of the Board, which is composed of two non-management Directors and one management Director. The Audit Committee meets with management and auditors to satisfy itself that management's responsibilities are properly discharged, to review the consolidated financial statements and to recommend approval of the consolidated financial statements to the Board.

The consolidated financial statements have been audited by PricewaterhouseCoopers in accordance with generally accepted auditing standards on behalf of the shareholders. The external auditors have full and unrestricted access to the Audit Committee and management to discuss matters arising from their audit, which includes a review of accounting records and internal controls. Their report dated January 10, 2003 outlines the scope of their examination and opinion on the consolidated financial statements.

John D. Mull

John D. Mull, M.D.
Chairman, President and Chief Executive Officer

Auditors' Report

To the Shareholders of Canadian Medical Laboratories Limited

We have audited the consolidated balance sheets of Canadian Medical Laboratories Limited as at September 30, 2002 and 2001 and the consolidated statements of income, retained earnings and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Company as at September 30, 2002 and 2001 and the results of its operations and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

Chartered Accountants

PricewaterhouseCoopers LLP

Mississauga, Ontario
January 10, 2003

Consolidated Balance Sheets

As at September 30, 2002 and 2001 (in thousands of dollars)	2002 $	2001 $
Assets (note 6)		
Current assets		
Cash and cash equivalents	26,706	19,558
Accounts receivable	23,113	14,983
Other current assets	2,177	1,428
Future income taxes (note 10)	3,178	553
Discontinued operations (note 3)	10,375	11,429
	65,549	47,951
Property and equipment (note 4)	16,549	6,223
Licences (note 15)	194,084	151,204
Goodwill (note 15)	5,027	5,027
Investments and other assets (note 5)	12,282	4,101
Due from related parties (note 12)	454	454
Discontinued operations (note 3)	854	25,808
	294,799	240,768
Liabilities		
Current liabilities		
Accounts payable and accrued liabilities	17,927	9,742
Deferred revenue	478	178
Income taxes payable	3,320	2,768
Current portion of long-term debt (note 6)	20,742	16,500
Discontinued operations (note 3)	16,971	4,741
	59,438	33,929
Long-term debt (note 6)	40,597	27,250
Future income taxes (note 10)	3,386	1,300
Discontinued operations (note 3)	-	1,796
	103,421	64,275
Shareholders' Equity		
Share capital (note 7)	63,823	61,069
Retained earnings	127,683	114,147
Cumulative translation adjustment	(128)	1,277
	191,378	176,493
	294,799	240,768

Contingencies and commitments (note 9)

John D. Mull

John D. Mull, M.D.
Director

S. Chepa

Steven W. Chepa
Director

Consolidated Statements of Income

For the years ended September 30, 2002 and 2001 (in thousands of dollars, except for per share amounts)	2002 $	2001 $
Revenue	232,448	164,841
Expenses		
Operating, general and administrative (note 12)	137,241	89,579
Research and development	9,728	757
Amortization of licences	-	4,246
Amortization of goodwill	-	1,327
Amortization of property and equipment	2,332	1,332
Amortization of other assets	28	684
	149,329	97,925
	83,119	66,916
Long-term interest	2,813	3,360
Income before income taxes	80,306	63,556
Provision for income taxes (note 10)	35,670	27,813
Income from continuing operations	44,636	35,743
Loss from discontinued operations (note 3)	(11,375)	(368)
Net income for the year	33,261	35,375
Basic earnings (loss) per share (note 8)		
Continuing operations	2.19	1.75
Discontinued operations	(0.56)	(0.02)
	1.63	1.73
Diluted earnings (loss) per share		
Continuing operations	2.17	1.72
Discontinued operations	(0.55)	(0.02)
	1.62	1.70

Consolidated Statements of Retained Earnings

For the years ended September 30, 2002 and 2001 (in thousands of dollars)	2002 $	2001 $
Retained earnings - Beginning of year, as previously reported	114,147	78,772
Change in accounting policy, impairment of goodwill of discontinued business (notes 1 and 3)	(19,725)	-
Retained earnings - Beginning of year, restated	94,422	78,772
Net income for the year	33,261	35,375
Retained earnings - End of year	127,683	114,147

Consolidated Statements of Cash Flows

For the years ended September 30, 2002 and 2001 (in thousands of dollars)	2002 $	2001 $
Cash provided by (used in)		
Operating activities		
Net income from continuing operations	44,636	35,743
Items not affecting cash		
Amortization	2,360	7,589
Future income taxes	4,018	(3,248)
Impairment in preference share	1,389	-
	52,403	40,084
Net change in non-cash working capital items (note 13)	(24)	(2,478)
Discontinued operations	(489)	(167)
	51,890	37,439
Investing activities		
Purchase of property and equipment	(1,535)	(1,020)
Purchase of property and equipment with a government grant	(9,210)	-
Increase in investments and other assets	(6,264)	(4,070)
Business acquisition - net of cash acquired (note 2)	(18,888)	(3,803)
Net proceeds from sale of discontinued operations	1,519	-
Decrease in due from related parties	-	720
Discontinued operations	(87)	(9,314)
	(34,465)	(17,487)
Financing activities		
Repayment of bank indebtedness	(4,083)	-
Principal repayment of long-term debt	(67,304)	(20,000)
Proceeds from issuance of long-term debt	49,250	-
Issuance of share capital (note 7)	2,754	-
Government grant received to purchase property and equipment	9,210	-
Discontinued operations	(104)	-
	(10,277)	(20,000)
Increase in cash and cash equivalents	7,148	(48)
Cash and cash equivalents - Beginning of year	19,558	19,606
Cash and cash equivalents - End of year	26,706	19,558
Supplementary information		
Interest paid	2,755	3,600
Income taxes paid	26,858	27,163

Notes to Consolidated Financial Statements

September 30, 2002 and 2001 (in thousands of dollars)

1 Summary of significant accounting policies

The consolidated financial statements have been prepared in accordance with Canadian generally accepted accounting principles.

Basis of consolidation

The consolidated financial statements include the accounts of the Company and its subsidiaries from their date of acquisition. All intercompany accounts and transactions with subsidiaries have been eliminated.

Translation of foreign currencies

The Company's U.S. operations, which have now been discontinued (note 3), were self-sustaining operations. Assets and liabilities of this Discontinued Business were translated at exchange rates in effect at the balance sheet date. Revenues and expenses were translated at average exchange rates prevailing during the year. Resulting unrealized gains or losses have been accumulated and reported as cumulative translation adjustment in shareholders' equity. Upon disposal of the final portion of the Discontinued Business, the balance in this account will be charged to loss from discontinued operations.

Revenues and expenses of the Company and its Canadian subsidiaries arising from foreign currency transactions are translated into Canadian dollars using the exchange rate in effect at the transaction date. Monetary assets and liabilities are translated using the rate in effect at the balance sheet date. Related exchange gains and losses are included in the determination of earnings.

Use of estimates

The preparation of the financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenue and expense during the reporting periods presented. Actual results could differ from the estimates.

Cash and cash equivalents

Cash and cash equivalents are defined as cash and short-term deposits with original maturities of three months or less.

Property and equipment

Property and equipment are recorded at cost, less accumulated amortization. Amortization is computed using the declining balance method and applies the following rates estimated to amortize the cost over the useful life of the assets:

Laboratory and diagnostic equipment	7% to 20%
Computer equipment	20%
Computer software	33.3%
Furniture and fixtures	10%
Leasehold improvements	20%

Government assistance

Government assistance received for the purchase of diagnostic equipment has been accounted for as a reduction in the cost of the diagnostic equipment.

September 30, 2002 and 2001 (in thousands of dollars)

Goodwill and licences

Goodwill represents the excess of the costs of the investment in acquired businesses over the fair value of the underlying assets assigned. The Company's licences are intangible assets with indefinite lives. These licences enable the Company to perform healthcare diagnostic services in Canada. Effective October 1, 2001, the Company adopted the new recommendations of the Canadian Institute of Chartered Accountants (CICA) Handbook Section 3062, Goodwill and Other Intangible Assets. In accordance with the requirements of the new standard, effective October 1, 2001, the Company is no longer amortizing its goodwill or licences. The need for any writedown of the goodwill and licences due to an impairment in their value is based on an assessment of the fair value of the individual business units and the related goodwill and licences. Any writedown of goodwill and licences arising from an impairment in value is recorded in the year in which the impairment is identified.

Upon adoption of the new standard, the Company assessed the fair value of the goodwill and licences. The Company has determined that as at October 1, 2001, there is no impairment in the value of the licences. The Company's assessment of the fair value of the goodwill indicated that $19,725 of goodwill was impaired as at October 1, 2001. In accordance with the requirements of the new standard, this goodwill impairment loss (all of which related to the discontinued operations discussed in note 3) was charged to retained earnings.

On a pro forma basis, the impact of adopting the new standard on prior year earnings is:

	2002 $	2001 $
Net income for the year	33,261	35,375
Addback: Licences and goodwill amortization	–	5,573
Adjusted net income for the year	33,261	40,948
Earnings per share	1.63	1.73
Licences and goodwill amortization	–	0.27
Adjusted earnings per share	1.63	2.00

Investments

Long-term investments are recorded at cost and are written down to their estimated recoverable amount if there is evidence of a decline in value, which is other than temporary.

Revenues

Revenues are recorded as laboratory and medical imaging services are provided to customers.

Revenue from long-term contracts related to the Company's pharmaceutical research segment is recognized using the percentage of completion method of accounting. Billings in excess of services performed to date are deferred.

The majority of the Company's laboratory services revenue is earned from The Ontario Ministry of Health (MOH). This revenue is recognized as services are performed based on a contract with the MOH.

The MOH has set certain limits on healthcare expenditures and set graduated limits on the amounts reimbursed for clinical laboratory services. To the extent that fees paid to private laboratories exceed the set limits, amounts received will have to be reimbursed. Each year, the repayment amounts, if any, are not determined until after the completion of the fiscal year-end of the Government of Ontario.

The Company has used the latest available information in estimating the amount of fees received that will have to be reimbursed. Assumptions were made with respect to the amount of reimbursement required and the volume and type of laboratory tests referred to the Company. It is possible that changes in future conditions in the near term could require a change in the amount to be reimbursed.

September 30, 2002 and 2001 (in thousands of dollars)

Income taxes

The Company follows the asset and liability method of accounting for income taxes whereby future income tax assets and liabilities are recognized based on the differences between the bases of assets and liabilities used for financial and income tax purposes. Future income tax assets are recognized only to the extent that management determines that it is more likely than not that the future income tax assets will be realized. Future income tax assets and liabilities are adjusted for the effects of changes in tax laws and rates on the date of enactment or substantive enactment. The income tax expense or benefit is the income tax payable or refundable for the year plus or minus the change in future income tax assets and liabilities during the year.

2 Business acquisitions

During 2002, the Company acquired two businesses (2001 - two businesses). These acquisitions have been accounted for as purchases and, accordingly, the financial statements include the results of operations of the acquired businesses from the dates of acquisition.

2002 business acquisitions

DC DiagnostiCare Inc.

Through a series of transactions completed during 2002, the Company acquired 100% of the issued and outstanding common shares of DC DiagnostiCare Inc. (DC) and 53,620,217 warrants to purchase 53,620,217 common shares of DC for total cash consideration, including acquisition costs of $18,844. The Company is in the process of restructuring and integrating the operations of DC with its Healthcare and Diagnostic segment. These restructuring and integration activities are expected to amount to $2,723. This amount has been reflected in the purchase price allocation. DC provides diagnostic medical imaging services to the Ontario, British Columbia, Alberta, Manitoba and Quebec markets.

The purchase price has been allocated to the fair value of the assets acquired and the liabilities assumed based on fair values.

The fair value of the net assets at the date of acquisition is as follows:

	$
Current assets	10,478
Long-term receivables and investments	848
Property and equipment	10,321
Licences	42,593
Future income taxes	4,557
Current liabilities	(14,994)
Long-term debt	(34,959)
Cash consideration paid	18,844

Other

Also during the year, the Company acquired one diagnostic clinic for cash consideration of $414. The net assets acquired comprised licences and diagnostic equipment.

September 30, 2002 and 2001 (in thousands of dollars)

2001 business acquisitions

Hartford Research Group Inc.

On October 4, 2000, the Company's wholly owned subsidiary, Summit Research Network (Ohio) LLC, acquired the assets of the Hartford Research Group Inc. (Hartford) for total consideration of $9,194 (excluding contingent consideration of $8,991). Hartford is a Site Management Organization, which centrally manages three research sites in Dayton, Ohio; Cincinnati, Ohio and Florence, Kentucky.

During the year, the Company discontinued its Site Management Organization business and completed the sale of Summit Research Network (Ohio) LLC (note 3). In accordance with the terms of the sale agreement, the Company will not be required to pay the contingent consideration described above.

The fair value of the net assets at the date of acquisition is as follows:

	$
Current assets	2,020
Property and equipment	207
Current liabilities	-
Goodwill	6,967
Cash consideration paid	9,194

Metro Medical Laboratories Limited

On June 15, 2001, the Company acquired substantially all of the laboratory assets of Metro Medical Laboratories Limited (Metro) for total consideration of $4,142. As at September 30, 2001, the operations of Metro had been fully integrated with those of the Healthcare and Diagnostic segment. Included in the purchase allocation was a restructuring reserve of $135. The restructuring reserve consisted primarily of severance costs related to the closing of Metro's laboratory facilities. The restructuring plan was completed by September 30, 2001.

The fair value of the net assets at the date of acquisition is as follows:

	$
Current assets	5
Licences	4,272
Current liabilities	(135)
	4,142

Consideration paid is as follows:

	$
Cash	3,803
Additional cash consideration paid during fiscal 2002	339
	4,142

Notes to Consolidated Financial Statements

September 30, 2002 and 2001 (in thousands of dollars)

3 Discontinued operations

On May 15, 2002, the Company adopted a formal plan of disposition related to its Site Management Organization (SMO) business (the Discontinued Business).

A portion of the Discontinued Business was disposed of on May 31, 2002 for cash proceeds of $1,572 and a note receivable of $3,174 (US$2,000). The note receivable bears interest at 4.75% per annum beginning December 1, 2002 and is due June 1, 2007. The required payments on this note are as follows: $100 due November 30, 2002 and quarterly payments of $85 commencing on March 1, 2003.

An additional portion of the Discontinued Business was disposed of on November 5, 2002.

The Company expects to exit the final portion of the Discontinued Business during 2003.

As a result of this plan of disposal, the results of operations for the Discontinued Business have been reported as discontinued operations and previously reported financial statements have been reclassified.

The summarized statements of income for the Discontinued Business are as follows:

	Oct. 1, 2001 to May 15, 2002 $	Year ended Sept. 30, 2001 $
Revenue	15,709	23,564
Operating, general and administrative expenses	16,353	22,846
Amortization	139	547
	(783)	171
Interest expense	4	440
	(787)	(269)
Recovery of income taxes	33	122
Loss before non-controlling interest	(754)	(147)
Non-controlling interest	33	221
Loss for the period	(721)	(368)
Provision for loss on sale of discontinued operations	(10,654)	-
Loss from discontinued operations	(11,375)	(368)

The cumulative translation adjustment, which is a separate component of shareholders' equity and which relates entirely to the Discontinued Business, will be expensed at the final date of disposition.

Notes to Consolidated Financial Statements

September 30, 2002 and 2001 (in thousands of dollars)

The summarized balance sheets for the Discontinued Business are as follows:

	2002 $	2001 $
Current assets		
Cash	1,836	561
Accounts receivable	7,689	10,489
Other current assets	465	368
Future income taxes	385	11
	10,375	11,429
Property and equipment	686	932
Goodwill	-	24,719
Other assets	168	157
	11,229	37,237
Current liabilities		
Accounts payable and accrued liabilities	4,469	2,850
Deferred revenue	670	1,115
Income taxes payable	1,178	776
Provision for loss on sale of discontinued operations	10,654	-
	16,971	4,741
Non-controlling interest	-	1,699
Future income taxes	-	97
	16,971	6,537
Net assets (liabilities)	(5,742)	30,700

As discussed in note 1, an assessment of the fair value of the goodwill was finalized during 2002, at which time it was determined that $19,725 of goodwill was impaired. In accordance with the requirements of the CICA, this goodwill impairment loss (all of which related to the Discontinued Business) was charged to retained earnings.

September 30, 2002 and 2001 (in thousands of dollars)

4 Property and equipment

			2002
	Cost $	Accumulated amortization $	Net $
Laboratory and diagnostic equipment	22,848	11,504	11,344
Computer equipment	6,437	4,683	1,754
Computer software	1,718	1,501	217
Furniture and fixtures	2,073	1,520	553
Leasehold improvements	6,056	3,375	2,681
	39,132	22,583	16,549

			2001
	Cost $	Accumulated amortization $	Net $
Laboratory and diagnostic equipment	12,713	10,178	2,535
Computer equipment	5,869	4,330	1,539
Computer software	1,637	1,431	206
Furniture and fixtures	1,837	1,456	381
Leasehold improvements	4,419	2,857	1,562
	26,475	20,252	6,223

September 30, 2002 and 2001 (in thousands of dollars)

5 Investment and other assets

	2002 $	2001 $
Galephar Pharmaceutical Research Inc. preferred shares (a)	5,816	3,443
Genetic Diagnostic Inc. (b)	2,750	250
DC DiagnostiCare Inc. deferred acquisition costs (note 2)	-	370
Note receivable (note 3)	3,174	-
Escrowed funds (c)	332	-
Notes receivable and other assets	210	38
	12,282	4,101

a) During 2001, the Company's wholly owned subsidiary, Cipher Pharmaceutical Ltd., entered into four agreements with Galephar Pharmaceutical Research Inc. (Galephar) to package, test, obtain regulatory approvals for and market certain products in North and South America, the Caribbean and Bermuda. In accordance with the terms of the agreements, the Company has invested $7,205 (US$4,625) (2001 - $3,443 (US$2,250)) in four separate series of preferred shares of Galephar, each of which is recoverable as a deduction from future licensing fees/royalties on the related products currently under development.

During 2002, it was determined that the Company's investment in the preferred shares related to Budesonide could be impaired and, therefore, a provision for the full amount of the investment of $1,389 was recorded in the year.

b) The Company's investment in Genetic Diagnostic Inc. (GDI) comprises 1,900,000 common shares (14% of the issued and outstanding common shares) of this research and development company. The Company's investment in GDI is accounted for on the cost basis of accounting.

c) The escrowed funds relate to the disposal of a business by DC prior to its acquisition by the Company. Any claims related to the disposal of the business will be withheld from the escrowed amount.

	$
Balance of escrow account at September 30, 2002	808
Less: Provision for claims	(237)
	571
Less: Current portion (included in accounts receivable)	(239)
Long-term portion due July 18, 2004	332

d) The fair value of the preferred shares cannot be determined due to the uncertainty of the timing of cash payments. The fair values of the note receivable and escrowed funds approximate the carrying value.

September 30, 2002 and 2001 (in thousands of dollars)

6 Long-term debt

	2002 $	2001 $
Revolving 364-day acquisition facility from Canadian Imperial Bank of Commerce and a syndicate of financial lenders extendible for a further 364-day period with consent of lenders. If not extended, the facility is repayable in quarterly instalments of $2,250 commencing April 15, 2003. Interest payable monthly in arrears at prime or bankers' acceptance rate plus 1.125%	38,000	10,750
Five-year term facility from Canadian Imperial Bank of Commerce and a syndicate of financial lenders. Matures March 31, 2004. Repayable in quarterly instalments of $3,000. Interest payable monthly in arrears at prime or bankers' acceptance rate plus 1.125%	21,000	33,000
Obligations under capital lease due in monthly payments through 2004	2,339	-
	61,339	43,750
Less: Current portion of long-term debt	(20,742)	(16,500)
	40,597	27,250

During the year, the Company increased its 364-day acquisition revolver financing facility by $15,000 to $60,000. This facility was used to finance the DC acquisition (note 2).

The Company also has a $10,000 operating loan facility bearing interest at the bank prime rate which, at year-end, had not been drawn down.

The operating loan and long-term debt are secured by:

i) first priority security interest in all of the assets and undertakings of the Company and its subsidiaries;

ii) first priority security interest in all accounts receivable, inventory, all trademarks, patents, licences, "corporate caps", and all other intellectual property of the Company and its subsidiaries;

iii) first priority pledge of all issued and outstanding common shares held by the Company in all subsidiaries; and

iv) an assignment in favour of material contracts and proceeds under insurance contracts.

The effective rate of interest for 2002 was 3.64% (2001 - 6.25%). The revolving and term facilities are represented by bankers' acceptances. The carrying value of the long-term debt at September 30, 2002 approximates its fair value.

The minimum principal repayments required in the next four years, with the conservative assumption that the revolving 364-day acquisition facility is not extended, are as follows:

	$
2003	20,742
2004	22,456
2005	16,141
2006	2,000
	61,339

7 Share capital

Authorized share capital

The authorized share capital consists of an unlimited number of preference shares, issuable in series, and an unlimited number of voting common shares.

Issued share capital

The following is a summary of changes in share capital during the last two years:

(all amounts are in thousands)	Common shares number	Common shares amount $
September 30, 2000 and 2001	20,407	61,069
Options exercised during 2002	540	2,754
September 30, 2002	20,947	63,823

September 30, 2002 and 2001 (in thousands of dollars)

Stock Option Plan

	2002	2001
Options outstanding at beginning of year	983	933
Options granted during the year	275	50
Options exercised during the year	(540)	-
	718	983

The weighted average exercise price per option is $21.48 (2001 - $12.20).

On November 14, 1996, the Board of Directors approved a stock option plan and reserved 1,700,000 shares in respect of this plan.

Employee stock options granted by the Company contain exercise prices, which are equivalent to the share price on the grant date. Any consideration paid by employees on exercise of stock options or purchase of stock is credited to share capital.

A summary of the stock options outstanding at September 30, 2002 is as follows:

		Number of options		
Expiry date	Exercise price $	Vested	Unvested	Total
August 9, 2004	21.50	260	-	260
December 15, 2005	22.00	123	-	123
October 12, 2008	6.35	-	10	10
February 22, 2011	17.55	35	15	50
January 11, 2012	22.50	110	165	275
		528	190	718

8 Earnings per share

Effective October 1, 2001, the Company adopted the new recommendations of the CICA Handbook Section 3500, Earnings per Share. Basic earnings per share are computed by dividing the income available for common shareholders by the weighted average number of common shares outstanding during the year. Diluted earnings per share are computed using the treasury stock method whereby the weighted average number of common shares used in the basic earnings per share calculation is increased to include the number of additional common shares that would have been outstanding if the dilutive potential common shares had been issued.

Earnings per share are calculated using the weighted average number of shares outstanding. The weighted average number of shares outstanding for the year ended September 30, 2002 was 20,424,293 (2001 - 20,407,252).

Diluted earnings per share reflect the dilutive effect of the exercise of stock options as disclosed in note 7. The number of shares for the diluted earnings per share calculation was 20,562,668 (2001 - 20,794,673).

Notes to Consolidated Financial Statements

September 30, 2002 and 2001 (in thousands of dollars)

9 Contingencies and commitments

Minimum lease commitments

Minimum lease commitments under operating leases for each of the next five years and thereafter are as follows:

	$
2003	15,097
2004	12,384
2005	9,134
2006	6,240
2007	3,074
Thereafter	7,248
	53,177

Legal proceedings

Various lawsuits and claims are pending against the Company. It is not possible to determine the merits of these claims or to estimate the possible financial liability, if any, to the Company. Accordingly, no provision has been made for these claims in these financial statements.

10 Income taxes

The effective income tax rate on consolidated earnings is influenced by items such as available losses carried forward and non-deductible expenses.

Future income tax assets (liabilities) of the Company are as follows:

	2002 $	2001 $
Differences in property and equipment asset basis	(10,248)	(1,980)
Accounting reserves not deducted for tax	1,256	553
Non-capital loss carry-forwards	12,835	825
Other	285	-
	4,128	(602)
Valuation allowance	(4,336)	(145)
	(208)	(747)
Future income tax asset	3,178	553
Future income tax liability	(3,386)	(1,300)
	(208)	(747)

September 30, 2002 and 2001 (in thousands of dollars)

The Company has $46,900 in non-capital loss carry-forwards at September 30, 2002, which are available to reduce future years' income taxes payable. These loss carry-forwards expire in varying amounts from 2005 to 2017.

A valuation allowance of $4,336 has been recorded to reduce the net benefit recorded in the financial statements related to the future tax assets. The valuation allowance is deemed necessary as a result of the uncertainty associated with the ultimate realization of these future tax assets. Of this amount, approximately $2,800 of the valuation allowance relates to pre-acquisition non-capital loss carry-forwards of DC. The realization in the future of any of these losses will result in a reduction of the DC licences.

	2002 %	2001 %
Combined Canadian federal and provincial statutory income tax rate	39.1	42.5
Increase (decrease) in statutory income tax rate resulting from the following		
Non-deductible amortization of licences and goodwill	-	2.1
Difference in foreign tax rate	3.1	-
Losses not recognized	1.5	0.8
Reduction in future income taxes resulting from reduction in enacted income tax rate	(0.1)	(1.7)
Other	0.8	0.1
Effective income tax rate	44.4	43.8

11 Financial instruments

Credit risk exposures

Financial instruments that potentially subject the Company to credit risk consist principally of cash and cash equivalents and accounts receivable. The Company places its cash with high credit quality financial institutions.

Credit risk with respect to accounts receivable is limited, as the majority of the receivable balance is due from the MOH and other government bodies.

Fair values of financial assets and liabilities

The fair values of cash and cash equivalents, accounts receivable and accounts payable and accrued liabilities approximate their carrying amounts included in the balance sheet due to the relatively short period of maturity of the instruments.

September 30, 2002 and 2001 (in thousands of dollars)

12 Related party transactions

In the normal course of business, the Company leases facilities from companies that are controlled by certain shareholders and officers of the Company. Rent expense of $1,322 (2001 - $1,374) related to these leased facilities, measured at the exchange amount, has been included in operating, general and administrative expenses.

At September 30, 2002, $454 (2001 - $454) is due from a company controlled by certain shareholders and officers of the Company. The fair value of the amounts due from related parties cannot be determined due to the uncertainty of the timing of cash payments. This balance consists of a gross receivable of $683 (2001 - $570), net of an allowance of $229 (2001 - $116). The Company is currently making regular mortgage payments on behalf of the related party. As at September 30, 2002, the related party's share of the outstanding mortgage to which these payments relate is $690. The Company has continued to fund these mortgage payments. The amount due from the related party will be repaid when the mortgaged property is sold.

13 Statement of cash flows

	2002 $	2001 $
Net change in non-cash working capital items comprises		
Accounts receivable	1,774	2,838
Other current assets	76	(69)
Accounts payable and accrued liabilities	(2,130)	(1,051)
Deferred revenue	300	(479)
Income taxes payable	(44)	(3,717)
	(24)	(2,478)

Notes to Consolidated Financial Statements

September 30, 2002 and 2001 (in thousands of dollars)

14 Segmented information

Industry segmentation

For purposes of operating decision-making and assessing performance, management considers that it operates within two dominant business segments: Healthcare and Diagnostic and Pharmaceutical Research. The Healthcare and Diagnostic segment consists of laboratory testing and medical imaging services in Ontario, British Columbia, Alberta and Quebec. The Pharmaceutical Research segment is engaged in the development of reformulated drug products, clinical trials and research that pharmaceutical companies have outsourced.

2002

	Healthcare and Diagnostic $	Pharmaceutical Research $	Consolidation entry $	Total per financial statements $
Revenue	227,131	5,579	(262)	232,448
Research and development	-	9,728	-	9,728
Amortization expense	1,924	436	-	2,360
Interest expense (income)	3,892	(1,079)	-	2,813
Tax expense	35,112	558	-	35,670
Net income (loss) from continuing operations	52,414	(8,382)	604	44,636
Property and equipment expenditures	1,413	122	-	1,535
Property and equipment	14,725	1,824	-	16,549
Total assets of continuing operations	321,762	24,970	(63,162)	283,570

2001

	Healthcare and Diagnostic $	Pharmaceutical Research $	Consolidation entry $	Total per financial statements $
Revenue	159,994	5,459	(612)	164,841
Research and development	-	757	-	757
Amortization expense	5,776	1,813	-	7,589
Interest expense	3,359	1	-	3,360
Tax expense (recovery)	28,525	(712)	-	27,813
Net income (loss) from continuing operations	39,787	(4,008)	(36)	35,743
Property and equipment expenditures	846	174	-	1,020
Property and equipment	4,785	1,438	-	6,223
Total assets of continuing operations	219,049	5,058	(20,576)	203,531

September 30, 2002 and 2001 (in thousands of dollars)

Geographic information

	2002 $	2001 $
Revenues**		
Canada	230,990	163,111
United States	1,458	1,730
	232,448	164,841
Property and equipment		
Canada	16,549	6,223
Goodwill		
Canada	5,027	5,027

** Revenues are attributable to countries based upon the location of the customer.

15 Licences and goodwill

Licences are net of accumulated amortization of $24,498 (2001 - $24,498). Goodwill is net of accumulated amortization of $1,864 (2001 - $1,864).

16 Comparative figures

Certain comparative figures have been reclassified to conform to the current year's presentation.

Board of Directors and Officers

John D. Mull, M.D., F.R.C.P. (C)
Chairman, President and
Chief Executive Officer

Kenneth R. Wiener
Secretary and Director
Partner, Goodmans LLP
Barristers and Solicitors

Paul J. Bristow, CA
Chief Financial Officer

Craig J. Mull
Director of Corporate Development

Steven Chepa
Director
President and CEO of Cheppa Corporation

Waldemar Zimmerman
Director
Barrister and Solicitor

Shareholder Information

Correspondence

For more detailed information about the Company, financial data and news releases, please visit the CML website at www.cmlhealthcare.com or contact Barry Hildred at The Equicom Group Inc.

(416) 815-0700 x 224 or

email: bhildred@equicomgroup.com.

Stock Exchange Listing and Symbol

CML's common shares are listed on the Toronto Stock Exchange under the trading symbol CLC.

Fiscal 2002 Common Share Price Performance

- High $34.10
- Low $17.70
- Closing Price $29.65 at September 30, 2002

Annual & Special Meeting

Date: March 26, 2003, 4:30 PM.

Place: TSE Conference Centre
The Exchange Tower,
2 First Canadian Place,
Toronto, Ontario

Shareholder Inquiries

Inquiries regarding change of address, transfer requirements or lost certificates should be directed to the Company's transfer agent.

Transfer Agent

CIBC Mellon Trust Company
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Toronto, Ontario
M5H 4A6

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Goodmans LLP

Auditors

PricewaterhouseCoopers LLP

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Fort Frances Clinic Holdings Limited

Pharma Medica Research Inc.

Novoquest Research, Inc.

Labcare Inc.

DC DiagnostiCare Inc.

Cipher Pharmaceuticals Limited

Canadian Medical Laboratories Limited

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